

CERI 2004 Electricity Conference

The Future of Restructuring

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There is no “right” model

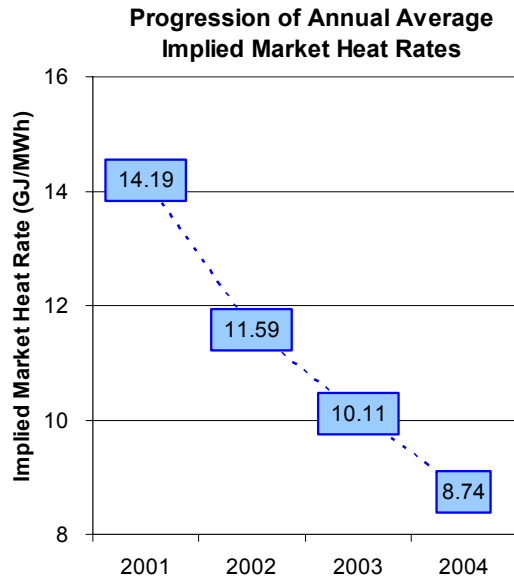
- Many models can work
- A great deal depends on where you start
- Human foibles are omnipresent!



Competent implementation of any model is key!

Re-Structuring so far – Alberta

- Consumers are much better off
- Major risk reallocation has taken place
- Supply adequate for now
- Supplier profitability low
- Future supply adequacy?



The free Lunch fantasy

- Artificially low power Prices?
- No Tax burden?
- No Public debt?
- Economic sustainability?



Pick any 3 of the 4! ...We can have almost anything we want... just not everything we want!

3 Premises of restructured markets

1. The essence of a restructured market is a price signal.
2. The market operator and all market participants are competent, and rational. Each act in their self interest per the market rules, guided by a price signal.
3. The optimal outcome for society should not depend on expecting or *forcing* participants to behave irrationally.

Seminal Question

- What is it about the nature of our price signal (or the rules, or interaction between rules and participants or between participants) that can cause individually optimal strategies to produce collectively sub-optimal results?

The answer(s) to this question gives the most useful insights into the maintenance needs of restructured markets.

Price signals drives behavior ...

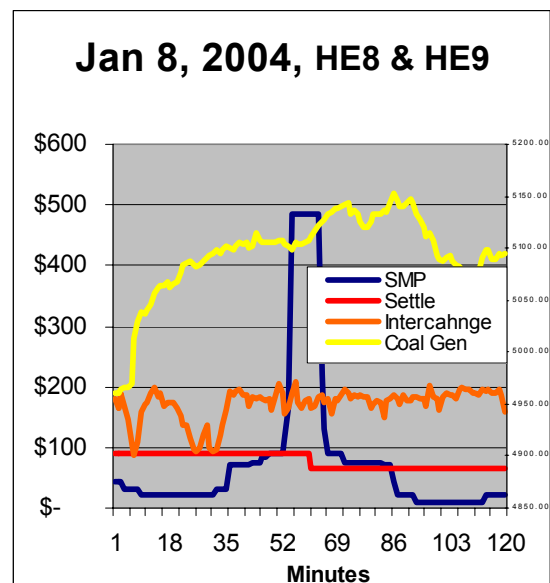
(or we get what we incent)

- **Dispatch on one price and settle on another**
 - ⇒ Have to offer \$500 to get \$250
- **Dispatch compliance**
 - ⇒ Participants don't get on/off when asked
 - ⇒ Don't produce what they're asked
 - ⇒ Some get on/off without ever advising or being asked
- **Unrevealed megawatts & negawatts**
 - ⇒ A logical risk/profit management strategy for participants
- **Steep supply curve**
 - ⇒ A byproduct of participants doing what they have to

These issues are connected, they are byproducts of the price signal! (that causes rational participants to produce sub-optimal results)

Price Fidelity

- Dispatched @ \$480, get \$90 for 20 minutes!
- Dispatched @ \$15, get \$90
- Unoffered, uncommanded coal creep
- Tie a non-factor



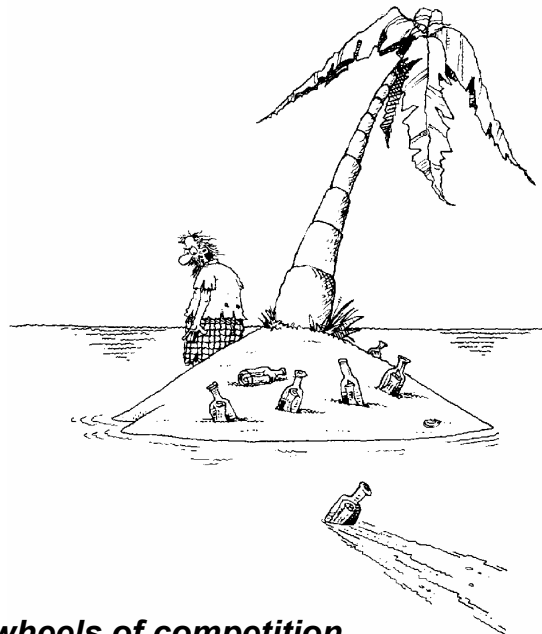
5 Themes for a Fair, Efficient and openly Competitive market

- Create an information rich environment
- Level the playing field
- Assure a high fidelity price signal
- Build confidence
- Let competition do the heavy lifting

Different than the path of many North American Monitoring Agencies

1. Information

- More is almost always better:
 - Efficiency
 - Transparency
 - Confidence
- MSA
 - Published Reports
 - Advocacy
 - TPG



Information greases the wheels of competition

2. Level Playing Field

- Aspects
 - Large v. small
 - Incumbent v. new entrant
 - Taxable v. not taxable
 - Supplier v. consumer
- Issues
 - Earned v. unearned
 - Intended v. unintended
- MSA
 - Analysis and Publication
 - Code of Conduct adjudication
 - Advocacy



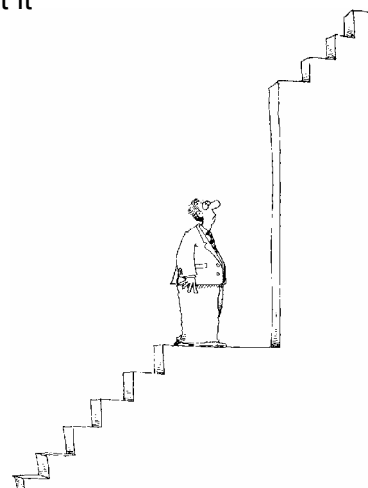
The quest for competitive advantage must not have unreasonable barriers

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Martin Merritt

3. High Fidelity Price signal

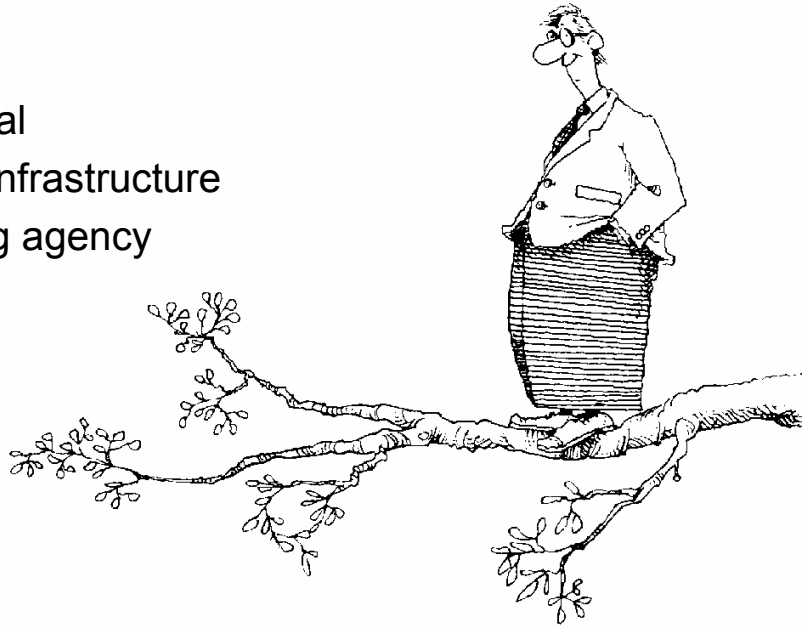
- The *essential premise* of a market...(without it we have nothing)
- Requires information rich and level field environment...(items 1 & 2)
- Requires attention to detail but is market structure independent
- MSA
 - Link to forward market signal – TPG
 - Tie line – uneconomic flows?
 - Impact of regulating reserve dispatch?
 - Impact of \$0 offers, self dispatch and load response?



Job #1 for any market monitoring agency

4. Build Confidence

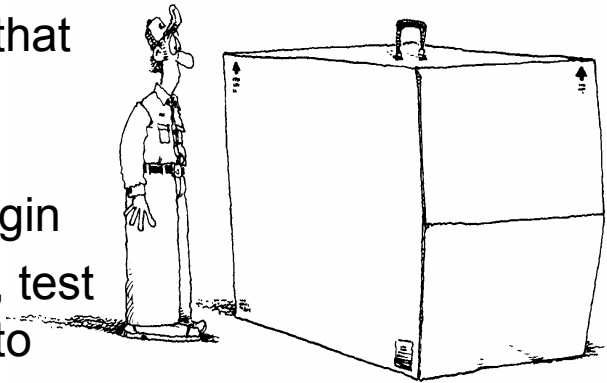
- In the price signal
- In the market's infrastructure
- In the monitoring agency
- MSA
 - Principled
 - Consistent
 - Light handed



Building confidence is not speedy or stealthy

5. Ensure Competition does the heavy lifting!

- Resist the urge to fix that which will fix itself
- Competition must be allowed a control margin
- Monitor, test, monitor, test monitor, test...return to step 1.



We are not the invisible hand, we are at best its assistant!

Summary

- There is no perfect model.
- Albertans are much better off than they would have been.
- Beware the free lunch
- Let's be sure this model can add capacity
- Focus on price signal fidelity.

